

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

JUNE 14, 2001

IN RE:

**PETITION OF LYNWOOD UTILITY CORPORATION
TO CHANGE AND INCREASE RATES AND CHARGES**

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**DOCKET NO.
99-00507**

**ORDER DENYING REQUEST FOR TARIFF CHANGE,
SETTING FORTH OPTIONAL IRRIGATION ADJUSTMENT,
AND CONCLUDING CONSIDERATION OF OUTSTANDING ISSUES**

This matter came before the Tennessee Regulatory Authority (the “Authority” or the “TRA”) at a regularly scheduled Authority Conference held on February 21, 2001, for consideration of the request for a tariff change (the “Request”)¹ filed on October 6, 2000 by Lynwood Utilities Company (“Lynwood” or the “Company”) and for final resolution of the remaining outstanding issue in this matter, the apparent over-billing of Lynwood’s only non-residential customer.

BACKGROUND

Lynwood filed a petition to change and increase rates and charges for sewer service on July 15, 1999. A Hearing was held on January 26, 2000. At the regularly scheduled Authority Conference held on February 29, 2000, Lynwood was granted a rate increase and a new billing system was approved for the Company in which residential customers would be billed based on the number of gallons of water they used rather than on the number of bedrooms in their homes,

¹ *Request for Tariff Change to Implement Sewer Bill Adjustment for Water Used for Irrigation and for Clarification of Order Approving Rate Increase for Non-Residential Customers*, Docket No. 99-00507, October 6, 2000.

which was Lynwood's previous method of billing. An Order reflecting the Authority's actions was entered on May 10, 2000. In approving Lynwood's request for a rate increase, the Authority held this docket open for further consideration of three issues: (1) the apparent over-billing of Lynwood's only non-residential customer, Walnut Grove Elementary School (the "School"); (2) the failure of either Lynwood's previous owner, Mr. David Terry, or Lynwood's current owner, Southern Utility Corporation ("Southern"), to obtain TRA approval of the transfer of Lynwood's authority to provide utility service which came about when Mr. Terry sold Lynwood to Southern in 1999; and (3) the alleged waiver of certain tap fees by Mr. Terry during his ownership of Lynwood.

After Lynwood implemented the rates approved in February 2000, the Company and the Authority received numerous complaints from Lynwood's customers concerning the new rates. Mr. Jacob C. (Chris) Martin, a Lynwood customer in the Cottonwood subdivision and spokesman for a group of customers, requested permission to intervene in this docket. At a regularly scheduled Authority Conference held on July 11, 2000, the Directors heard testimony from Mr. Martin, State Representative Charles Sargent, and Mr. Randolph Jones. The Authority granted Mr. Martin intervention as to the three outstanding issues, but not as to the rate increase.² The Authority also received numerous letters and facsimiles voicing concern about the size of the rate increase as well as a petition from customers located in the Legends Ridge subdivision. In particular, customers complained of receiving unreasonably high sewer bills from Lynwood because of heavy usage of water for irrigation. Because this water use is not related to sewer

² See *Order Denying Petition for Reconsideration and Granting Limited Intervention by Jacob C. (Chris) Martin*, Docket No. 99-00507, August 2, 2000. Mr. Martin was not granted intervention as to the rate increase because the Authority had already conducted its hearing and rendered its decision as to that issue. Mr. Martin has been served with copies of all documents subsequently filed in Docket No. 99-00507 and in Docket No. 00-00690, which addresses Lynwood's request for approval of the transfer of authority.

service, the customers contended that water used for irrigation should not be included in calculating the customers' sewer charges.

A second Hearing was held in this matter on August 2, 2000 to hear testimony on the three outstanding issues. On July 28, 2000, Lynwood filed a pre-hearing brief which set forth the provisions of a proposed agreement between Lynwood and Mr. Terry regarding the waived tap fees.³ The agreement provides for payment by Mr. Terry to Lynwood in the amount of \$138,000 on or before June 30, 2001, pursuant to a promissory note secured by a deed of trust on an unimproved lot in the Legends Ridge Subdivision. At the Hearing, Lynwood president Mr. Davis Lamb testified that there are no encumbrances on this lot and agreed to provide title insurance documents related to the lot. These documents were entered into the record as a late-filed exhibit.⁴

The Authority also heard testimony regarding billing for the School. Lynwood originally requested a rate increase for the School from \$1.40 per 1,000 gallons of water usage, which was Lynwood's longstanding non-residential tariff rate, to \$7.21 per 1,000 gallons of water usage. During the hearing on the rate increase in January 2000, Mr. Lamb could not explain how the School's initial rate had been determined. In a late-filed exhibit, Lynwood reported that the School was not being billed based on water usage but was actually being charged a flat rate of \$787.50 per month. This flat rate exceeded what the School would have paid if it were charged according to Lynwood's tariff rate. Mr. Lamb stated in the late-filed exhibit that he did not know how the flat rate was determined or how long it had been applied.⁵

³ At the August 2, 2000 Hearing, Mr. Terry admitted that some tap fees were "neglected" or "overlooked," and that other tap fees were knowingly waived for the sake of consistency. Transcript of Proceedings, Docket No. 99-00507, August 2, 2000, p. 23.

⁴ *Late Filed Exhibit 1*, Docket No. 99-00507, August 8, 2000.

⁵ *Lynwood's Response to Fourth Information Request*, Docket No. 99-00507, February 8, 2000, pp. 1-2.

At the August 2, 2000 Hearing, Mr. Lamb testified that the School had apparently paid the \$787.50 rate since it became a Lynwood customer, although he did not know when that was. Mr. Terry produced documents which showed that the School had paid the \$787.50 rate at least since 1992.⁶ Mr. Terry testified that he charged the School the same amount as had the previous owner from whom he bought the Company in 1996, and that he never discussed the rate with the School.⁷

Documents submitted by Mr. Lamb after the August 2, 2000 Hearing contradict Mr. Lamb's testimony and show that a rate of \$735 per month was established for the School when it became a Lynwood customer, based on applying Lynwood's non-residential tariff rate of \$1.40 per 1,000 gallons of water usage to an estimate of the School's monthly water usage.⁸ Nevertheless, for reasons unknown to Mr. Lamb the School paid Lynwood a flat rate of \$787.50 per month.

During the August 2, 2000 Hearing, the Authority heard testimony regarding the failure of Mr. Terry and Lynwood's current owners to obtain TRA approval for the transfer of authority to provide utility services which resulted when Mr. Terry sold Lynwood to Southern in 1999. At the Hearing, the Authority directed Lynwood to submit a petition for approval of the transfer. On August 7, 2000, Lynwood submitted its petition for approval *nunc pro tunc* of the transfer, which was assigned TRA Docket No. 00-00690.

At the regularly scheduled Authority Conference held on November 7, 2000, the Directors unanimously approved the agreement between Lynwood and Mr. Terry as the

⁶ *Billing History of Walnut Grove Elementary, Provided by David Terry in Response to Subpoena Duces Tecum*, Docket No. 99-00507, August 2, 2000.

⁷ Transcript of Proceedings, Docket No. 99-00507, August 2, 2000, pp. 16-17.

⁸ *Lynwood's Response to Authority Staff Data Request*, Docket No. 99-00507, October 19, 2000, pp. 2-3 and Attachment 4A, Letter from Michael A. Cochrane to Ronald Crucher, April 27, 1989.

resolution of the waived tap fee issue and reaffirmed a rate for the School of \$7.21 per 1,000 gallons, capped at the School's current flat rate of \$787.50 per month. The Directors also unanimously approved, in Docket No. 00-00690, the transfer of authority from Mr. Terry to Lynwood's current owners.⁹

LYNWOOD'S REQUEST FOR TARIFF CHANGE

Lynwood's Proposal of an Irrigation Adjustment

In its Request filed on October 6, 2000, Lynwood asks the Authority for approval to make an adjustment to its wastewater bills for water used by its customers for irrigation purposes. Lynwood proposes the following change to its tariff:

When a customer experiences high water usage as defined in this paragraph caused by irrigation for the April through September billing periods of any year, the Corporation [Lynwood] will make an adjustment to the sewer bill for irrigation. To obtain an irrigation adjustment, the customer must meet the following conditions:

1. The customer must request the irrigation adjustment;
2. The customer's water usage for the monthly billing period in which an adjustment is requested must exceed 1.25 times the average monthly water usage of the customer's premises for the preceding October through March billing periods. In the event the customer's premises has not been receiving water and sewer service for the previous October through March billing periods, the Corporation shall use the average monthly water usage for the previous October – March billing periods for a typical customer in the same subdivision for calculating the adjustment;
3. The customer's average monthly water usage during the October – March billing periods must be at least 8000 gallons;
4. The customer's high water usage must be caused by irrigation; and
5. The customer must be current in the payment of customer's account for sewer service.¹⁰

⁹ See *Order Approving Transfer of Authority Nunc Pro Tunc*, Docket No. 00-00690, January 24, 2001.

¹⁰ *Request for Tariff Change*, Docket No. 99-00507, October 6, 2000, pp. 4-5.

Lynwood's Proposal to Use Tap Fee Settlement Funds to Offset Revenue Losses

In its Request, Lynwood states that it estimates that the implementation of the proposed wastewater bill adjustment for irrigation will result in a decrease in annual revenues of approximately \$66,500.¹¹ This figure is based on actual water usage records for Lynwood's customers from October 1999 through March 2000. The Company estimates that 561 customers would be entitled to such bill adjustments. After the Request was filed, Lynwood submitted a revised figure showing an annual reduction of \$52,106.60.¹² To recover the lost revenue, Lynwood proposes to use funds it will receive from the tap fee settlement with Mr. Terry. Lynwood does not address how any lost revenue would be replaced once the settlement funds are exhausted but does intend to continue with the irrigation adjustment at that time.

FINDINGS AND CONCLUSIONS

The Directors considered Lynwood's Request during a regularly scheduled Authority Conference held on February 21, 2001. Based upon the entire record in this proceeding, the Authority made the following findings and conclusions.

Proposed Irrigation Adjustment

The irrigation adjustment proposed in Lynwood's Request includes several conditions. The customer must request the rate; average winter usage is used to estimate non-irrigation summer usage; each month's summer usage must exceed winter usage by twenty-five percent (25%); and the winter usage must be greater than 8,000 gallons per month. While the Authority

¹¹ Lynwood states in its Request that

The loss of revenue resulting from the implementation of the sewer adjustment rule is a concern to Lynwood. According to the test year adopted in the rate case, the revenues to be produced by the rates approved still do not allow it to cover its operating expenses and depreciation expense and permit it to earn the 8% rate of return approved by the Authority. The loss of additional revenue from the irrigation adjustment could worsen Lynwood's financial condition.

Request for Tariff Change, Docket No. 99-00507, October 6, 2000, p. 5.

¹² *Lynwood Amended Revenue Calculation*, Docket No. 99-00507, October 26, 2000.

agrees with Lynwood that an adjustment is necessary, the Authority rejects Lynwood's proposal because it does not make the irrigation adjustment available to all of its customers and thus could result in an unlawful discriminatory charge or preference in violation of Tenn. Code Ann. § 65-4-122.¹³

Because a fairly high differential between summer and winter usage is a prerequisite to participation in the bill adjustment, a number of Lynwood's customers will be unable to receive any adjustment for water use attributable to irrigation. This is not only discriminatory as to the individual customer, but given the usage patterns of Lynwood's customers, would have the effect of generally favoring one of Lynwood's subdivisions, Legends Ridge, over another, Cottonwood, without any separately justifiable basis for doing so. The same is true of Lynwood's proposed requirement that the customer's average monthly winter consumption must be above 8,000 gallons. This clearly excludes any customer whose winter consumption is below that level whether or not that customer is paying for irrigation usage during the selected months.

The Authority does not find fault with Lynwood's goal of making an appropriate adjustment for irrigation or with Lynwood's basic approach, which is to base the irrigation adjustment on the difference between winter and summer usage. This approach is common in wastewater rate design. The Authority finds, however, that Lynwood's adjustment, as proposed would result in discriminatory treatment of customers and therefore concludes that Lynwood's Request should be denied. The Authority finds that a more equitable arrangement would be a

¹³ Tenn. Code Ann. § 65-4-122(a) provides

If any common carrier or public service company, directly or indirectly, by any special rate, rebate, drawback, or other device, charges, demands, collects, or receives from any person a greater or less compensation for any service within this state than it charges, demands, collects or receives from any other person for service of a like kind under substantially like circumstances and conditions, and if such common carrier or such other public service company makes any preference between the parties aforementioned such common carrier or other public service company commits unjust discrimination, which is prohibited and declared unlawful.

billing system in which Lynwood's customers would be billed for the period between April 1 and October 31 based on their average monthly consumption of water between November 1 and March 31 or their actual water usage, whichever is less, with no minimum usage requirement. Furthermore, the adjustment should be automatic. Should Lynwood determine to implement an irrigation adjustment, Lynwood may refile its tariff consistent with this billing method.

Revenue Loss and Use of Tap Fee Settlement Funds

The Authority recognizes that any irrigation adjustment, whether the one proposed by Lynwood or the one recommended herein by the Authority, may result in a revenue reduction. Although the Authority disagrees with Lynwood's assertions as to its ability to earn its authorized rate of return,¹⁴ the Authority agrees with Lynwood's proposal to use the tap fee settlement to offset any revenue reductions that may be caused by an irrigation adjustment. Normally, a company would use tap fee revenues to offset initial plant cost. In this instance, however, the Authority finds that allowing Lynwood to use funds from the tap fee settlement to offset revenues lost as a result of an irrigation adjustment will benefit Lynwood's customers by allowing improvements to continue in Lynwood's daily operations. Therefore, the Company will be allowed to use the tap fee settlement, up to a maximum of \$138,000, to offset the effect of the irrigation adjustment should Lynwood choose to implement such an adjustment. Any additional funds realized from the sale of the security property or the settlement should go to offset plant cost.

In addition, should Lynwood choose to refile its tariff to implement an irrigation adjustment as recommended by the Authority, Lynwood shall prepare a notice to its customers,

¹⁴ In its May 10, 2000 Order, the Authority approved, but did not guarantee, a rate of return for Lynwood. Lynwood's protestations that it is unable at present to meet its approved rate of return should not deter the Company from implementing a billing mechanism that may have the effect of reducing its revenues.

subject to Authority approval, describing the changes in billing methods that are approved by the Authority. Within thirty (30) days after the new billing system is approved, the notice shall be mailed to each customer currently receiving service from the Company. The notice may be included with customers' monthly bills.

The Overbilling of Walnut Grove Elementary School

In its Request, Lynwood states that the Company is uncertain as to the rate for the School which the Authority approved on February, 2000 and which is reflected in its May 10, 2000 Order. "Because of the uncertainty about what rate Lynwood should be charging the school," the Request states, "Lynwood has continued to charge the school \$787.50 per month regardless of usage."¹⁵ The Request further states that

Lynwood seeks a clarification from the Authority on the rate it should be charging the school. Lynwood suggests that the Authority approve the flat rate of \$787.50 which the school has been paying for several years. The school's monthly sewer bill is subject to wide variation depending on whether children are in school during the month of service. This rate will maintain the school's revenue contribution to Lynwood which will not have to be picked up by residential customers. This rate will also permit the school to better budget its monthly sewer costs.¹⁶

At the November 7, 2000 Authority Conference, the Directors made clear that in approving Lynwood's Petition for a rate increase in February 2000, the Authority approved a non-residential rate of \$7.21 per 1,000 gallons, to be capped at \$787.50 per month. In addition, the Directors unanimously reaffirmed the non-residential rate for Lynwood as \$7.21 per 1,000 gallons, capped at \$787.50 per month.¹⁷

¹⁵ *Request*, Docket No. 99-00507, October 6, 2000, p. 8. The Request raises other issues, having particularly to do with a proposed adjustment in customer bills to allow for water used for irrigation purposes, that are not addressed in this Order.

¹⁶ *Id.*, pp. 8-9.

¹⁷ Transcript of Authority Conference, November 7, 2000, pp. 13-14. See *Order Reaffirming Non-Residential Rate and Approving Tap Fee Agreement*, Docket No. 99-00507, May 2, 2001.

With regard to the issue of whether the School was over-billed, the Authority unanimously concluded at the February 21, 2001 Authority Conference that the record supports a factual finding that the School was not charged in excess of its initial rate. Instead, the Company failed to amend its tariff to reflect the rate actually being charged to the School. The Authority appropriately investigated the discrepancy between the Company's non-residential tariff rate and the rate actually charged the School. As a result of that investigation, the Authority concludes that Lynwood did not, based on its cost and rate structure, "collect[] or receive[] more than a just and reasonable rate of toll or compensation for service" and therefore did not violate Tenn. Code Ann. § 65-4-122(b).

Consequently, the Authority finds that any punitive, corrective, or disciplinary action is not warranted. While Lynwood failed to have a current tariff on file, this failure did not result in the Company realizing revenue or charging a rate to the School that was unjust and unreasonable. The issue of the over-billing of the School being thus resolved, the Authority determined that the three outstanding issues in this docket, as set forth in the May 10, 2000 Order, have been concluded and that this docket may be closed.

Based on careful consideration of Lynwood's Request, and of the entire record in this matter, the Directors voted unanimously at the February 21, 2001 Authority Conference to deny Lynwood's Request. Instead, the Directors set forth an acceptable alternative irrigation adjustment which the Company may choose to implement. The Directors voted unanimously to allow the Company to treat funds received from its tap fee settlement with Mr. Terry as revenues to offset to a maximum amount of \$138,000 any decrease in revenues that may result from the implementation of an irrigation adjustment, but only in the event the Company implements an

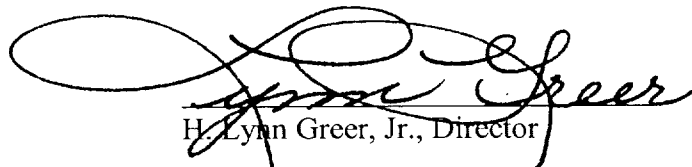
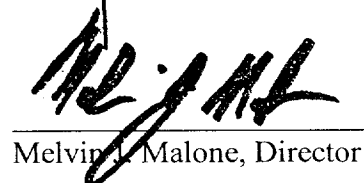
irrigation adjustment. The Directors determined not to take disciplinary action against Mr. Terry or Lynwood's current owners with regard to the over-billing of the School.

IT IS THEREFORE ORDERED THAT:


1. Lynwood Utility Corporation's Request for a Tariff Change is denied;
2. Lynwood may refile a tariff to provide an irrigation adjustment, i.e. an adjustment in customer bills for water usage for purposes not related to wastewater service, provided that any such adjustment should contain no minimum usage requirement, that the adjustment should be handled in such a way that each customer is billed for each month between April 1 and October 31 at the customer's average monthly water usage for the period from November 1 to March 31 or the customer's actual usage for that particular month, whichever is lower and that the adjustment should automatically apply to all customers;
3. Should Lynwood refile its tariff to provide an irrigation adjustment as set forth above, Lynwood may use funds received from the tap fee settlement, approved by the Authority on November 7, 2000, to the limit of \$138,000, as revenues for the sole purpose of offsetting any revenue losses resulting from implementation of an irrigation adjustment as set forth in paragraph 2, above;
4. In addition, should Lynwood refile its tariff to implement an irrigation adjustment as specified in paragraph 2, above, Lynwood shall prepare a notice to its customers, subject to Authority approval, describing the changes in billing methods that are approved by the Authority, such notice to be mailed to each customer currently receiving service from the Company within thirty (30) days after a new billing system is approved;
5. The Authority shall take no action against David Terry or Lynwood's current owners with regard to the Company's billing practices for Walnut Grove Elementary School;

6. Any party aggrieved with the Authority's decision in this matter may file a Petition for Reconsideration with the Authority within fifteen (15) days from the date of this Order; and

7. Any party aggrieved with the Authority's decision in this matter has the right of judicial review by filing a Petition for Review in the Tennessee Court of Appeals, Middle Section, within sixty (60) days from and after the date of this Order.


Sara Kyle, Chairman
H. Lynn Greer, Jr., Director
Melvin L. Malone, Director

ATTESTED:


K. David Waddell, Executive Secretary